

CITY OF BLAINE
Whatcom County, Washington
January 1, 1993 Through December 31, 1993

Schedule Of Findings

1. The City Should Avoid Making Gifts Of Public Funds

During our review of the city we noted the following instances of the city making a gift of public funds:

- a. The city passed an ordinance for the surplus of community center assets owned by the city. This ordinance stipulated the assets could be sold by the Senior Association, a nonprofit organization, and the proceeds from the sale of the assets were to be deposited in the city's Community Center Construction Fund. Funds from the sale of the assets were never deposited in the fund and the city was unable to provide documentation of the assets sold or the amount of money received from the sale.
- b. The city is not currently in possession of assets purchased for the Marine Center. City officials indicated these assets are in the possession of private citizens who are members of the Marine Foundation, a private nonprofit organization.

The *Constitution of the State of Washington*, Article VII, Section 7, states in part:

No county, city, town or other municipal corporation shall hereafter give any money, or property, or loan its money, or credit to or in aid of any individual, association, company or corporation, except for the necessary support of the poor and infirm

The city's failure to establish controls to adequately monitor the use and disposition of city assets and ensure prompt payment for assets disposed of results in a direct violation of the state constitution and the possible loss of revenue for the city.

We recommend the city establish procedures to ensure assets are properly safeguarded and the city is properly compensated for any assets disposed of. (See also Federal Finding.)

2. The City Should Ensure One Fund Does Not Provide Benefit To Another Without Proper Compensation

During our audit we noted the Public Works Engineering Fund charged the city's utility funds on a percentage basis for all of its budgeted operating costs. However, the Engineering Fund performs work not only for the utility funds, but also for Local Improvement Districts, other city construction funds, and other funds as needed. In 1993, because engineering charged and received payments from funds in addition to the utility funds, the Engineering Fund ended up with a cash surplus of approximately \$85,513. The utility funds were not reimbursed this excess amount until January 1994.

RCW 43.09.210 states in part:

. . . no department, public improvement, undertaking, institution, or public service industry shall benefit in any financial manner whatever by an appropriation or fund made for the support of another.

City officials failed to require the Engineering Fund to promptly reimburse the utility funds for their portion of engineering costs paid from other sources. This resulted in the Engineering Fund having excess cash to invest, thereby earning interest revenue at the expense of the utility funds.

We recommend city officials implement a system to ensure interfund charges are based on actual or historical costs, so each fund pays the appropriate amount for services provided.

3. The City Should Adhere To Bid Requirements

During our review of the city we noted bid requirements had not been complied with in two instances:

- a. The city failed to follow competitive bid procedures for the purchase of fuel in the amount of \$27,303 for resale at the airport.
- b. In November 1993, the city's light crew performed work for the Blaine School District. The actual labor performed by the city was less than \$20,000 but the school district purchased all materials for the project, causing the total project costs to exceed the \$20,000 ceiling for one craft project.

RCW 35A.40.210 states in part:

Procedures for any public work or improvement contracts or purchases for code cities shall be governed by the following statutes, as indicated:

(2) For code cities under twenty thousand population; RCW 35.23.352.

RCW 35.23.352 states in part:

(1) Any second or third class city or any town may construct any public works, as defined in RCW 39.04.010, by contract or day labor without calling for bids therefor whenever the estimated cost of the work or improvement, including cost of materials, supplies and equipment will not exceed the sum of thirty thousand dollars if more than one craft or trade is involved with the public works, or twenty thousand dollars if a single craft or trade is involved with the public works or if the public works project is for street signalization or street lighting . . .

Whenever the cost of the public work or improvement, including materials, supplies and equipment, will exceed these figures, the same shall be done by contract. All such contracts shall be let at public bidding upon posting notice calling for sealed bids upon the work . . . The council or commission of the city or town shall let the contract to the lowest responsible bidder . . .

(6) Any purchase of supplies, material, equipment or services other than professional services, except for public work or improvement, where the cost thereof exceeds seven thousand five hundred dollars shall be made upon call for bids: PROVIDED, That the limitations herein shall not apply to any purchases of materials at auctions conducted by the government of the United States, any agency thereof or by the state of Washington or a political subdivision thereof.

RCW 39.09.020 states in part:

In addition to any other remedies or penalties contained in any law, municipal charter, ordinance, resolution or any other enactment, any municipal officer by or through whom or under whose supervision, in whole or in part, any contract is made in wilful and intentional violation of any law, municipal charter, ordinance, resolution or other enactment requiring competitive bidding upon such contract shall be held liable to a civil penalty of not less than three hundred dollars and may be held

liable, jointly and severally with any other such municipal office, for all consequential damages to the municipal corporation. If, as a result of a criminal action, the violation is found to have been intentional, the municipal officer shall immediately forfeit his office

Noncompliance with bid requirements appeared to be the result of the city's failure to establish and implement proper bid policies and procedures, and departmental personnel's unfamiliarity with bid requirements.

By failing to call for competitive bids, the city is denying the business community the opportunity to bid for the contracts and cannot assure the public that they are getting the lowest possible price. Without established policies and procedures or proper controls over contracts, the opportunities for error and/or abuse are increased.

We recommend the city's management implement bid policies and procedures which comply with legal requirements and ensure that those policies and procedures are complied with.

4. The City Should Restrict Fund Expenditures To Authorized Budget

The city made expenditures which exceeded approved budget appropriations in city funds in 1993 as follows:

Central Blaine Sewer Project \$494,093

RCW 35A.33.120 states in part:

The expenditures as classified and itemized in the final budget shall constitute the city's appropriations for the ensuing fiscal year. Unless otherwise ordered by a court of competent jurisdiction, and subject to further limitations imposed by ordinance of the code city, the expenditure of city funds or the incurring of current liabilities on behalf of the city shall be limited to the following:

(1) The total amount appropriated for each fund in the budget for the current fiscal year . . .

(4) Funds received in excess of estimated revenues during the current fiscal year, when authorized by ordinance amending the original budget . . .

(5) Expenditures required for emergencies

In addition, RCW 35A.33.125 states:

Liabilities incurred by any officer or employee of the city in excess of any budget appropriations shall not be a liability of the city. The clerk shall issue no warrant and the city council or other authorized person shall approve no claim for an expenditure in excess of the total amount appropriated for any individual fund, except upon an order of a court of competent jurisdiction or for emergencies as provided in this chapter.

Expenditures in excess of budgeted authorizations resulted from the failure of city officials to monitor expenditures in relation to budgeted appropriations and the failure to adopt budget amendments prior to making expenditures in excess of the original budget.

By incurring expenditures in excess of appropriations, city officials are circumventing the budgetary process, preventing citizens' input prior to expenditure, and violating state law.

We recommend the city develop and implement a system of controls which will prevent expenditures in excess of budget authorizations. This should include effective budget monitoring and timely budget amendments

5. Local Improvement District Accounting Should Be Improved

The city does not have control totals for local improvement districts' assessments receivable. Control totals are a necessary part of a receivable system to provide additional assurance that all transactions pertaining to customer accounts have been properly recorded.

The city has not utilized control totals in the past several years due to time constraints, changes in the city's computerized accounting system, and changes in personnel who account for local improvement districts.

Failure to maintain an assessments receivable control total results in a significantly greater risk that errors or irregularities could occur and not be detected in a timely manner. In addition, increased audit costs result from the additional audit effort necessary to review the special assessment transactions.

We recommend city officials:

- a. Establish control totals for local improvement districts' assessments receivable.
- b. Reconcile subsidiary receivable ledgers to the control account on a periodic basis by someone other than the person handling the local improvement districts' receivables.

6. The City Should Improve Controls Over Public Works Materials And Supplies Inventory

During a special audit of the Public Works Department for 1991 and 1992, we noted several weaknesses in the materials and supplies inventory control system. Over the past year, city officials have made improvements in some areas, but have failed to address the following critical areas:

- a. There are no written policies and procedures relating to the access to, issuance of, and accounting for inventory items.
- b. Responsibility for inventory has been fixed, but proper safeguards over inventory are not in place.
- c. The current system does not ensure that supplies and materials are charged at the correct prices to projects and does not provide accurate information with which to determine if loss or theft of inventory has occurred.
- d. Reconciliations are not performed which would allow management to monitor the effectiveness of the controls implemented, and identify weaknesses in the system.

RCW 43.09.200 Division of Municipal Corporations - Uniform System of Accounting states in part:

The accounts shall show the receipt, use, and disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source: all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transaction (Emphasis added.)

The American institute of Certified Public Accountants (AICPA) in its *Codification of Statements on Auditing Standards*, AU Section 319, Appendix D, states in part:

Establishing and maintaining an internal control structure is an important management responsibility. In establishing specific internal control structure policies and procedures concerning an entity's ability to record, process, summarize and report financial data that is consistent with management's assertions embodied in the financial statements, some of the specific objectives management may wish to consider include the following:

- a. Transactions are executed in accordance with management's general or specific authorization.
- b. Transactions are recorded as necessary (1) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria to such statements and (2) to maintain accountability of assets.
- c. Access to assets is permitted only in accordance with management's authorization.
- d. The recorded accountability for assets is compared with existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

Access to Assets

The objective of safeguarding assets requires that access be limited to authorized personnel. In this context, access to assets includes both direct physical and indirect access through the preparation or processing of documents that authorize the use or disposition of assets. Access to assets is required in the normal operations of a business and, therefore, limiting access to authorized personnel is the maximum feasible constraint. The number and competence of personnel to whom access is authorized should be influenced by the nature of the assets and the related susceptibility to loss through errors and irregularities. Limitation of direct access to assets requires appropriate physical segregation and protective equipment or devices. (Emphasis added.)

Management has failed to implement basic accounting controls, making it difficult to hold individuals responsible or accountable for their own activities. As a result, inventory is not adequately safeguarded to discourage theft and other irregularities or to discover those occurrences in a timely manner. In addition, accounting records cannot be relied upon to determine the accurate costs of inventory, costs charged to projects, or to support the preparation of financial statements.

We recommend city officials improve controls over inventory as follows:

- a. Continue to develop comprehensive written policies and procedures relating to access to, issuance of, and accounting for inventory items.
- b. Provide individuals who have the responsibility for inventory the ability to control access to inventory.
- c. Establish basic inventory accounting procedures to control the issuance, return and use of inventory, and to ensure the proper pricing of supplies and materials to projects performed.
- d. Perform timely reconciliations of inventory supply and charges to other funds to help monitor the effectiveness of the controls implemented.

7. The City Public Works Department's Work Order System Needs To Be Strengthened

During our review of the city's work order system as part of a special audit of the Public Works Department covering 1991 and 1992, we noted several weaknesses. During a follow up performed in the current audit we noted improvements had been made in implementing one system for all of public works and ensuring all work orders are processed in a more timely manner. However, we noted the following weaknesses still exist:

- a. There is a lack of written policies and procedures relating to work orders.
- b. The current computerized work order system does not interface with the current accounting software.
- c. Procedures are inadequate to ensure all materials, time, and vehicles usage are charged on work orders or that all charges to the work order system are supported by payroll reports.
- d. Fixed asset usage rates lack supporting documentation. (See Finding 5.)

RCW 39.04.070, Public Contracts and Indebtedness - Account and Record of Cost, states:

Whenever the state or any municipality shall execute any public work by any means or method other than by contract or small works roster, it shall cause to be kept and preserved a full, true and accurate account and record of the costs of executing such work in accordance with the budgeting, accounting, and reporting system provisions prescribed by law for the state agency . . . (Emphasis added.)

Management has failed to implement basic accounting systems to provide accurate accounting for work performed. As a result, the city cannot ensure all costs are charged or support all charges to projects. In addition, with the condition of the fixed asset system as noted in the federal finding, the city cannot ensure accurate costs are charged with respect to vehicle rental rates. In addition, accounting records cannot be relied upon to determine the accuracy of costs charged to projects, or to support the preparation of financial statements.

We recommend the city implement an adequate work order control system.

CITY OF BLAINE
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Schedule Of Federal Findings

1. The City Should Improve Its Accounting For Fixed Assets

As noted in prior audit reports, the city's controls over fixed assets are inadequate. We noted that the city does not maintain a comprehensive fixed asset detail ledger or take a comprehensive annual physical inventory.

Because of the absence of adequate accounting procedures and controls, the city is not properly safeguarding public fixed assets. Furthermore, the city does not have adequate information to:

- a. Fix responsibility for custody of its assets.
- b. Provide adequate insurance coverage.
- c. Determine proper depreciation expense for the proprietary funds.
- d. Plan an effective replacement and maintenance program.
- e. Identify fixed assets acquired with federal funds and the final disposition of such property.

RCW 43.09.200, Division of Municipal Corporations - Uniformed system of accounting, states in part:

The accounts shall show the receipt, use, and disposition of all public property

RCW 43.09.200 also requires the State Auditor to prescribe the uniform accounting systems. The State Auditor prescribes the *Budgeting, Accounting, and Reporting System* (BARS) manual which states, in Volume 1, Part 3, Chapter 7, page 7:

Accountability for fixed assets is required of all local governments, regardless of size.

The Light Utility Fund uses the Federal Energy Regulatory Commission's (FERC) *Uniform System of Accounts for Public Utilities and Licensees* prescribed by the State Auditor in accordance with RCW 43.09.200. General instruction No. 2(a) in this prescribed system of accounts states that:

Each utility shall keep its book of accounts, and all other books, records, and memoranda which support the entries in such book of accounts as to any item included in any account.

Additionally, for any fixed assets purchased by the city using federal funds, the Office of Management and Budget (OMB) "Common Rule," section .32, [d] Management

requirements states in part:

- (1) Property records must be maintained that include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property.
- (2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.
- (3) A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft should be investigated.

Furthermore, generally accepted accounting principles require accounting for fixed assets and related depreciation.

In previous years city officials were reluctant to allocate the financial resources necessary to establish an adequate system of accounting for its fixed assets. In 1990, the city contracted with an appraisal company to inventory and appraise the utility funds' fixed assets; however, the data obtained from the appraisal was not utilized promptly to update the fixed asset records. The Public Works Department has recently initiated the process of performing a physical inventory of fixed assets and implementing a system to record and track those assets.

Because the city does not account for its fixed assets, there is an increased risk that errors or irregularities may occur and not be detected in a timely manner, if at all. In addition, we are unable to verify the accuracy of fixed assets, accumulated depreciation, and depreciation expense as presented in the financial statements of the Light Utility.

We again recommend that city officials continue their efforts to establish a fixed asset accounting system and conduct annual physical inventories of fixed assets.